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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-85220; File No. SR-NYSEArca-2019-06]

### **Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing of Proposed Rule Change to Amend Commentary .01 to NYSE Arca Rule 8.600-E Relating to Generic Listing Standards for Managed Fund Shares Applicable to Holdings in Fixed Income Securities**

February 28, 2019

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (the “Act”)<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that, on February 14, 2019, NYSE Arca, Inc. (the “Exchange” or “NYSE Arca”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### **I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change**

The Exchange proposes to amend Commentary .01(b)(5) to NYSE Arca Rule 8.600-E relating to a generic listing standards for Managed Fund Shares applicable to holdings in fixed income securities. The proposed change is available on the Exchange’s website at [www.nyse.com](http://www.nyse.com), at the principal office of the Exchange, and at the Commission’s Public

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

Commentary .01 to NYSE Arca Rule 8.600-E sets forth generic listing standards for listing and trading of Managed Fund Shares on the Exchange.<sup>4</sup> The Exchange proposes to amend Commentary .01(b)(5) to Rule 8.600-E, as described below.<sup>5</sup>

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<sup>4</sup> A Managed Fund Share is a security that represents an interest in an investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1) (the "1940 Act") organized as an open-end investment company or similar entity that invests in a portfolio of securities selected by its investment adviser consistent with its investment objectives and policies. In contrast, an open-end investment company that issues Investment Company Units, listed and traded on the Exchange under NYSE Arca Rule 5.2-E(j)(3), seeks to provide investment results that correspond generally to the price and yield performance of a specific foreign or domestic stock index, fixed income securities index or combination thereof.

<sup>5</sup> The Commission approved the generic listing standards in Commentary .01 to NYSE Arca Rule 8.600-E in Securities Exchange Act Release No. 78397 (July 22, 2016), 81 FR 49320 (July 27, 2016) (SR-NYSEArca-2015-110) (Order Granting Approval of Proposed Rule Change, as Modified by Amendment No. 7 Thereto, Amending NYSE Arca Equities Rule 8.600 to Adopt Generic Listing Standards for Managed Fund Shares).

Proposed Amendment to Commentary .01(b)(5) to Rule 8.600-E

Commentary .01(b) to NYSE Arca Rule 8.600-E sets forth generic listing standards applicable to fixed income securities included in the portfolio of a series of Managed Fund Shares.<sup>6</sup> Commentary .01(b)(5) provides that non-agency, non- GSE and privately-issued mortgage-related and other asset-backed securities (“ABS” and, collectively, “non-agency ABS”) components of a portfolio shall not account, in the aggregate, for more than 20% of the weight of the fixed income portion of the portfolio. The Exchange proposes to amend Commentary .01(b)(5) by deleting the words “fixed income portion” to provide that such 20% limitation would apply to the entire portfolio rather than to only the fixed income portion of the portfolio. Thus, Commentary .01(b)(5) would provide that non-agency, non-GSE and privately-issued mortgage-related and other ABS components of a portfolio shall not account, in the aggregate, for more than 20% of the weight of the portfolio.

The Exchange believes this amendment is appropriate because a fund’s investment in non-agency, non-GSE and privately-issued mortgage-related and other ABS may provide a fund with benefits associated with increased diversification, as such investments may be less correlated to interest rates than many other fixed income securities. The Exchange notes that application of the 20% limitation only to the fixed income portion of a fund’s portfolio may impose a much more restrictive percentage limit on permitted holdings of non-agency ABS for funds that have a more diversified investment portfolio than for funds that hold principally or

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<sup>6</sup> Commentary .01(b) provides that fixed income securities are debt securities that are notes, bonds, debentures or evidence of indebtedness that include, but are not limited to, U.S. Department of Treasury securities (“Treasury Securities”), government-sponsored entity securities (“GSE Securities”), municipal securities, trust preferred securities, supranational debt and debt of a foreign country or a subdivision thereof, investment grade and high yield corporate debt, bank loans, mortgage and asset backed securities, and commercial paper.

exclusively fixed income securities. For example, a fund holding 100% of its assets in fixed income securities can hold 20% of its entire portfolio's weight in non-agency ABS. In contrast, a fund holding 25% of its assets in fixed income securities, 25% in U.S Component Stocks, and 50% in cash and cash equivalents is limited to a 5% ( $25\% \times 20\% = 5\%$ ) allocation to non-agency ABS. The Exchange, therefore, believes application of the 20% limitation to a fund's entire portfolio would be more equitable for Managed Fund Shares issuers with different investment objectives and holdings.

In addition, a fund's investment in non-agency, non-GSE and privately-issued mortgage-related and other ABS will be subject to a fund's liquidity risk management program as approved by a fund's board of directors.<sup>7</sup> The liquidity procedures generally include public disclosure by funds of their liquidity and redemption practices. A fund's holdings in non-agency ABS would be encompassed within a fund's liquidity risk management program. To the extent a fund's procedures facilitate its ability to meet its redemption obligations, they may reduce potential manipulation of a fund's shares by promoting an efficient redemption mechanism for exchange-traded funds, including funds that hold non-agency ABS.

The Exchange notes that the Commission has previously approved the listing of actively managed exchange-traded funds that can invest 20% of their total assets in non-U.S.

Government, non-agency, non-GSE and other privately issued ABS and mortgage-backed

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<sup>7</sup> Rule 22e-4(b) under the 1940 Act requires, among other things, that a fund "adopt and implement a written liquidity risk management program that is reasonably designed to assess and manage its liquidity risk." The rule is "designed to promote effective liquidity risk management throughout the open-end investment company industry, thereby reducing the risk that funds will be unable to meet their redemption obligations and mitigating dilution of the interests of fund shareholders." See Release Nos. 33-10233; IC-32315; File No. S7-16-15 (October 13, 2016).

securities (“MBS”).<sup>8</sup> In addition, the Commission has previously approved listing and trading of shares of an issue of Managed Fund Shares where such fund’s investments in non-U.S. Government, non-agency, non-GSE and other privately issued ABS will, in the aggregate, not exceed 20% of the total assets of the fund, rather than the weight of the fixed income portion of the fund’s portfolio.<sup>9</sup> Therefore, the Exchange believes it is appropriate to apply the 20% limitation to a fund’s investment in non-agency, non-GSE and privately-issued mortgage-related and other ABS components of a portfolio in Commentary .01(b)(5) to a fund’s total assets.

The Exchange believes the proposed amendments would provide issuers of Managed Fund Shares with additional investment choices for fund portfolios for issues permitted to list and trade on the Exchange pursuant to the Rule 19b-4(e), which would enhance competition among market participants, to the benefit of investors and the marketplace.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,<sup>10</sup> in general, and furthers the objectives of Sections 6(b)(5) of the Act,<sup>11</sup> in particular,

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<sup>8</sup> See, e.g., Securities Exchange Act Release Nos. 80946 (June 15, 2017) 82 FR 28126 (June 20, 2017) (SR-NASDAQ-2017-039) (permitting the Guggenheim Limited Duration ETF to invest up to 20% of its total assets in privately-issued, non-agency and non-GSE ABS and MBS); 76412 (November 10, 2015), 80 FR 71880 (November 17, 2015) (SR-NYSEArca-2015-111) (permitting the RiverFront Strategic Income Fund to invest up to 20% of its assets in privately-issued, non-agency and non-GSE ABS and MBS); 74814 (April 27, 2015), 80 FR 24986 (May 1, 2015) (SR-NYSEArca-2014-107) (permitting the Guggenheim Enhanced Short Duration ETF to invest up to 20% of its assets in privately-issued, non-agency and non-GSE ABS and MBS); 74109 (January 21, 2015), 80 FR 4327 (January 27, 2015) (SR-NYSEArca-2014-134) (permitting the IQ Wilshire Alternative Strategies ETF to invest up to 20% of its total assets in MBS and other ABS, without any limit on the type of such MBS and ABS).

<sup>9</sup> See Securities Exchange Act Release No. 83319 (May 24, 2018), 83 FR 25097 (May 31, 2018) (SR-NYSEArca-2018-15) (Order Approving a Proposed Rule Change, as Modified by Amendment No. 1 Thereto, to Continue Listing and Trading Shares of the PGIM Ultra Short Bond ETF Under NYSE Arca Rule 8.600-E).

<sup>10</sup> 15 U.S.C. 78f(b).

because it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to, and perfect the mechanisms of, a free and open market and a national market system and, in general, to protect investors and the public interest and because it is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Exchange has in place surveillance procedures that are adequate to properly monitor trading in series of Managed Fund Shares in all trading sessions and to deter and detect violations of Exchange rules and applicable federal securities laws. The Exchange notes that the Exchange or Financial Industry Regulatory Authority (“FINRA”), on behalf of the Exchange, or both, would communicate as needed regarding trading in Managed Fund Shares with other markets and other entities that are members of the Intermarket Surveillance Group, and the Exchange or FINRA, on behalf of the Exchange, or both, could obtain trading information regarding trading in Managed Fund Shares from such markets and other entities. In addition, the Exchange could obtain information regarding trading in Managed Fund Shares from markets and other entities that are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement.

With respect to the proposed amendment to Commentary .01(b)(5), the Exchange believes this amendment is appropriate because a fund’s investment in non-agency, non-GSE and privately-issued mortgage-related and other ABS may provide a fund with benefits associated with increased diversification, as such investments may be less correlated to interest

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<sup>11</sup> 15 U.S.C. 78f(b)(5).

rates than many other fixed income securities. As noted above, application of the 20% limitation to only the fixed income portion of a fund's portfolio may impose a much lower percentage limit on permitted holdings of non-agency ABS for funds that have a more diversified investment portfolio than for funds that hold principally or exclusively fixed income securities. The Exchange, therefore, believes application of the 20% limitation to a fund's entire portfolio would be more equitable for Managed Fund Shares issuers with different investment objectives and holdings.

In addition, a fund's investment in non-agency, non-GSE and privately-issued mortgage-related and other ABS will be subject to a fund's risk management program as approved by a fund's board of directors, as required by Rule 22e-4 under the 1940 Act, which requires investment companies, including in-kind exchange-traded funds, to adopt a liquidity risk management program.<sup>12</sup> The liquidity procedures generally include public disclosure by funds of their liquidity and redemption practices. A fund's holdings in non-GSE and privately-issued mortgage-related and other ABS would be encompassed within a fund's liquidity risk management program. To the extent a fund's procedures facilitate its ability to meet its redemption obligations, they may reduce potential manipulation of a fund's shares by promoting an efficient redemption mechanism for exchange-traded funds, including those that hold non-agency ABS.

The Exchange notes that the Commission has previously approved the listing of actively managed exchange-traded funds that can invest 20% of their total assets in non-U.S. Government, non-agency, non-GSE and other privately issued ABS and MBS.<sup>13</sup> In addition, the Commission has previously approved listing and trading of shares of an issue of Managed Fund

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<sup>12</sup> See note 7, supra.

<sup>13</sup> See note 8, supra.

Shares where such fund's investments in non-U.S. Government, non-agency, non-GSE and other privately issued ABS will, in the aggregate, not exceed more than 20% of the total assets of the fund, rather than the weight of the fixed income portion of the fund's portfolio.<sup>14</sup> Therefore, the Exchange believes it is appropriate to apply the 20% limitation to a fund's investment in non-agency, non-GSE and privately-issued mortgage-related and other ABS components of a portfolio in Commentary .01(b)(5) to a fund's total assets.

The proposed rule change is designed to perfect the mechanism of a free and open market and, in general, to protect investors and the public interest in that it will facilitate the listing and trading of additional types of Managed Fund Shares that will enhance competition among market participants, to the benefit of investors and the marketplace.

B. Self-Regulatory Organization's Statement on Burden on Competition

In accordance with Section 6(b)(8) of the Act,<sup>15</sup> the Exchange believes that the proposed rule change would not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change would permit Exchange listing and trading under Rule 19b-4(e) of additional types of Managed Fund Shares, which would enhance competition among market participants, to the benefit of investors and the marketplace.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within

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<sup>14</sup> See note 9, supra.

<sup>15</sup> 15 U.S.C. 78f(b)(8).



such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NYSEArca-2019-06 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSEArca-2019-06. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications

relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NYSEArca-2019-06 and should be submitted on or before **[INSERT DATE 21 DAYS FROM PUBLICATION IN THE *FEDERAL REGISTER*]**.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>16</sup>

**Eduardo A. Aleman,**

*Deputy*

*Secretary.*

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<sup>16</sup> 17 CFR 200.30-3(a)(12).

